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April 8, 2005

Mr. Robert E. Feldman
Executive Secretary
Federal Deposit Insurance Corporation
550 17th Street, N.W.
Washington, D.C. 20429

Dear Bob:

As you know, I am not someone who has regularly commented on proposed regulation since my departure from the FDIC Board of Directors. However, I do attempt to stay informed and abreast of trends and developments in the banking regulatory arena. Being back in the industry, I can fully appreciate the burden that continuous, excessive regulatory expansion heaps upon the individual banker. This is disproportionately true for community banks and bankers.

In this regard, I must comment in regard to the interagency proposal on the classification of commercial credit exposures. Sometimes, an issue such as this comes along to make one think that regulatory creation and restructuring has become an industry unto itself Sadly, there are people housed within the agencies today whose sole purpose is to propose new or modified regulations such as this. Put simply, these people just don't have enough to do.

During my tenure as Director at FDIC, I was pleased to serve as Chairman of the Corporation's Community Development and Regulatory Improvement Act (CDRI) Clearing Committee. Our goal was to engage a top-to-bottom review of the Corporation's 120 existing regulations and policy statements in an attempt to streamline and simplify wherever possible The task was monumental and required significant time and effort by staff throughout the organization. The process and results were as gratifying as any undertaken during my tenure at FDIC. Our task force recommended either rescinding or revising 90 of the 120 regulations and policy statements. The Board affirmed our recommendations and recommended adoption by other regulatory counterparts on an interagency basis. We actually improved efficiency, reduced cost and burden, and removed outdated and duplicative requirements. It was refreshing to see staff eagerly adopt and endorse such a reversal of "business as usual".

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The proposal to change the classification of commercial credit exposures is totally unnecessary, particularly in community banks. Much banking regulation and policy begins with good intentions. Then it builds internal momentum and takes on a life of its own. (see Sarbanes-Oxley, BSA, etc.) By the time it reaches the industry, it has evolved into a multi-faceted, monolithic document that bears little resemblance to its former self.

This proposal serves to take a little more of the discretion and reasonableness out of the hands of the field examiner. By comparison, a dangerous and slippery slope was created with the passage of FDICIA, a well-intentioned piece of legislation intended to address industry health and solvency after the stormy 1980's. Certain elements of FDICIA were appropriate and rational, such as the creation of risk-based premiums for deposit insurance However, features of the prompt corrective action and least cost resolution sections of FDICIA, although timely and well-intended, eliminated discretion, creativity, and forbearance by the bank's supervisor. The regional or field examiner was typically closest to the problem, knew management, and had a greater sense for the institution's potential for recovery Under FDICIA, every situation was to be treated the same with little supervisory opportunity to use expertise gained by years of working within the industry in both good times and bad. Bank examiners and their supervisors in the field were denied the opportunity to use a valuable tool – good judgment. Former FDIC Chairman Bill Taylor once stated that there was no substitute for good judgment. He was asked, "How do you get good judgment?" He responded, "from experience". When asked "How do you get experience? ", he responded, "From bad judgment". There will never be a substitute for common sense and good judgment. The current classification system serves its purpose well if examiners utilize good judgment

The initial stated justification for this new proposal states that the current classification system dates back to 1938. What possible difference does that make? Should we now redraft regulation and policy in a chronological sequence? In its defense, this loan classification standard has been established, widely recognized, and understood by regulators, bankers, and bank directors for 67 years. Bank regulators currently have the ultimate authority to extensively discuss credits with bankers, assign ratings, allocate exposure, require reserves against that exposure, and take other precautionary measures as they see fit, including informal or formal enforcement actions. This proposal only serves to make someone in Washington feel better about themselves.

The second stated justification for this proposal is that it clarifies issues that have historically led to ratings differences between bankers and examiners. Clarifies? Surely, even a bureaucrat can't believe this. Someone is suggesting that this new two-dimensional framework will clarify a system that has been established and in place for 67 years?

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While at FDIC, I had the opportunity to weigh in on the interagency expansion of CAMEL to CAMELS. I voted against this for two reasons. First, I felt that the risk sensitivity assessment could easily be incorporated into the Liquidity component of CAMEL. More importantly, I voted against it because I was concerned for where this expansion may lead. CAMEL, much like the current loan classification system, had been widely understood and accepted by bankers, regulators, and bank directors for many years. My fear was that we could be headed for CAMELIZATION, or worse, if left to the whims of those whose existence depends upon such matters.

In 1938, we had a simpler tax code. Lou Gehrig played baseball because he loved the game. Common sense and good judgment were more prevalent than today. And, Orson Wells broadcast *War of the Worlds*, spreading panic by suggesting that aliens had landed. The regulatory community does not need to spread unnecessary panic claiming that this standard which has served bankers, regulators and bank directors well since 1938 should be replaced. There are simply more important things to do

Sincerely,

Joseph H. Neely
President and CEO